APPENDIX A.

Excerpt from Testimony of Hon. Robert P. Patterson, Under Secretary of War, before Committee on Banking and Currency, United States Senate, 77th Cong. 2d sess. on S. 2250, a Bill to Mobilize the Productive Facilities of Small Business in the Interests of Successful Prosecution of the War, and for Other Purposes, Part 2, March 20, 1942, page 329.

Statement of Hon. Robert P. Patterson, Under Secretary of War, Washington, D. C.

Mr. Patterson: We have given study of the pending bill introduced by Senator Murray and the other Senators conferring with him.

We now have under way a formula or plan for the financing of subcontractors and supplies which has been given careful study by the Army, the Navy, the Maritime Commission, and the War Production Board, as well as the Federal Reserve System.

We have never had a problem in financing prime contractors because Congress gave us authority in 1940 to finance them up to 30 percent by advance payments, and that has been extended. So far as the 30-percent limit is concerned, it has been removed under the First War Powers Act.

The problem has remained that of financing subcontractors, small as well as large—all kinds. In emergencies we have done it by giving the funds to the prime contractor on advances, with directions to extend it down the line, and we have even absolved them in some cases from liability, although I must confess that that was stretching, perhaps, what an advance payment means; but the need was very urgent in the case in which I authorized it.

We have also, in line with trying to get subcontractors financed through prime contractors, authorized all of our district officers in the procurement agencies of the War Department to make advances over and above the conventional 30 percent in cases where the contractor would agree to finance the subcontractors.

Senator Brown: That is, 30 percent of the over-all price in the contract?

Mr. Patterson: Yes; but we have agreed to go beyond that with the prime contractor if he will pass the funds down to his own subcontractors. Of course, that does not solve the problem, for the reason that you sometimes get quite a chain of them—sub-subs.

Also, a concern—a particular subcontractor—will have orders from prime contractors for the Army and also for the Navy, and you can't handle it in a very complete way by doing that.

We believe that the system that is now being formulated, and which we think will take effect very shortly under a proposed Executive order, which we think is perfectly proper under the First War Powers Act, whereby Army and Navy funds already appropriated for supplies can be used to take the risk of loss in advances made to subcontractors by the regular banking connections of those subcontractors, will be a satisfactory one.

The bill pending before the committee, as I understand it, so far as its financial provisions are concerned, limits the relief granted to loans of less than $100,000.

Senator Taft: No; that is wrong.

Mr. Patterson: Is that out?

Senator Taft: That is Mr. Jones' suggestion. He wants to limit it to $100,000. We have in our bill no limit except the capital of the corporation.

Mr. Patterson: I suggest that that amount of the loan should be limited by the need of the company and not by any set sum of money. We have concerns that, oh, 2 years

ago did a business of $50,000 a year and have on their books orders for $10,000,000. I am speaking particularly of concerns making indispensable parts for aircraft. They are small in a way, but in the volume of business we expect them to do they are not small. They are not direct contractors with us; if they were, we could handle the whole thing very readily. They are concerns—subcontractors—that make parts for aircraft assemblies.

Senator Taft: Judge Patterson, do you need legislation to authorize the War Department to say to a contractor, "You must advance so much to a subcontractor, and we will stand the risk of loss"? Do you need specific legislation for that? If so, it could be added to this bill very easily, if the War Department needs that.

Mr. Patterson: It would have been to advantage last summer, certainly, to have had that, because that would be routing in advance to a subcontractor through a prime contractor, as an advance payment to the prime contractor.

I think if we have full power to make loans—they are not advances, because we don't deal with them—loans to subcontractors who need additional working capital, and if that system will be perfected, as I think it will be very shortly, I do not know that we would need that. It would do no harm to have it.

Senator Taft: Without legislation, how will the War Department have that power to make loans to subcontractors?

Mr. Patterson: We would not make the loans. We would take the risk, however, and we would indemnify the Federal Reserve bank, which in turn would participate in it with local banks, or even guarantee a local bank where the subcontractor needed the money and where the Army, the Navy, or the particular procuring agency certified to the need.

Senator Taft: One of Mr. Jones' amendments here authorizes the War Department to guarantee the R. F. C.

against loss. It does not say anything about authorizing the guaranteeing of Federal Reserve banks against loss. Should they be added?

Mr. Patterson: The Executive order we would like to have would authorize us as to any lending agency, and that would include the R. F. C., the Federal Reserve banks, or local banks.

Senator Taft: You think that it may be done under the First War Powers Act?

Mr. Patterson: Yes, sir.

Senator Taft: The contract provision?

Mr. Patterson: Yes, sir. I myself have not studied it carefully, but the lawyers in the War Department, in the Navy Department, and in the War Production Board are all agreed on that.

Senator Taft: I should seriously doubt it, but there may be other provisions that I do not know about. In any event, you are not asking for it?

Mr. Patterson: We view it as primarily a procurement problem.

Senator Taft: You are not asking for legislation, then?

Mr. Patterson: No, sir.

Senator Taft: You think you can get what you want by Executive order?

Mr. Patterson: And very swiftly; yes.

Senator Taft: Do you think you need this provision of Mr. Jones', at the end of his amendment, which says this:

> The Departments of War and Navy are hereby authorized to participate in or to guarantee any loans made by the Reconstruction Finance Corporation pursuant to this provision, and they may use any funds heretofore or hereafter made available for purposes of procuring war materials, supplies, and equipment in connection therewith.

Do you think that is necessary?

Mr. Patterson: It would do no harm, but I suggest, if it is going to be touched upon, that it might be a proper provision to say—

> through the Reconstruction Finance Corporation, through the Federal Reserve banks, or through any other selected banking institutions.

Senator Taft: Your suggestion does not cover the question of trying to convert a number of small plants into pools of materials, and so forth?

Mr. Patterson: It will assist, of course, in financing.

Senator Taft: It is only to finance the actual contract? It does not cover the question of making big loans to a plant to buy machinery?

Mr. Patterson: That would be included.

Senator Taft: Buying machinery?

Mr. Patterson: Yes.

Senator Brown: You have heretofore done that?

Mr. Patterson: Yes, through the Defense Plant Corporation. The problem on financing, I believe, is to give those concerns that have been quite small, concerns that are now called upon to do a great volume of business, working capital. That is the way it is always reported to us; they need working capital.

Senator Taft: That does not really mean that. What you have largely done is to buy machinery and put it in through the War Department?

Mr. Patterson: Yes; through the Defense Plant Corporation.

Senator Taft: Always through the Defense Plant Corporation? Do you not have some independent appropriations?

Mr. Patterson: We have these concerns that employed 50 men 2 years ago but now employ 5,000 men. They need working capital very badly. That is where the problem comes. It is a very pressing problem.

Senator Taft: It only comes to you after the prime contractor has got the contract and says he wants to see it advanced?

Mr. Patterson: He will be making an indispensable part of some aircraft assembly. That is the reason why it is difficult to make an advance through a prime contractor. Some will say, "Yes; I am willing to take a chance on advancing money to this fellow," but others will not want to do it.

APPENDIX B.

Announcement concerning War Financing by Board of Governors of the Federal Reserve System published in Federal Reserve Bulletin, April, 1942, page 424.

War Financing.

Regulation V.

Pursuant to the authority contained in Executive Order No. 9112 of March 26, 1942, published at page 299 of the April 1942 Federal Reserve Bulletin, the Board of Governors of the Federal Reserve System adopted, effective April 6, 1942, Regulation V entitled "War Financing." The text of the Board's press release and of Regulation V is as follows:

STATEMENT FOR THE PRESS.

April 10, 1942.

The Board of Governors of the Federal Reserve System announced today adoption of Regulation V to carry out the President's Executive Order No. 9112 of March 26, 1942, for the purpose of facilitating and expediting the financing of war production. The Regulation was adopted after consultation with the War Department, the Navy Department, and the United States Maritime Commission following conferences in which representatives of the War Production Board participated.

The objective, as set forth in Regulation V, is to facilitate and expedite production for war purposes by arranging for the financing of contractors, subcontractors and others engaged in businesses or operations deemed by the armed services and the Maritime Commission to be necessary for the prosecution of the war.

The War Department has sent initial instructions to the Federal Reserve Banks covering the authority and procedure to be followed by them in acting for the War Department under the Board's Regulation. The program embraces financial aid for contractors and subcontractors, both large and small, and contemplates the maximum participation of small business enterprises in war production.

Regulation V prescribes general rules and policies to govern the operations of the twelve Federal Reserve Banks, which will act as fiscal agents of the armed services and the Maritime Commission in carrying out the President's Executive Order. The utilization of the facilities of the twelve Federal Reserve Banks and their twenty-four branches throughout the United States makes it possible to decentralize the war financing program to a large extent. The program looks to the fullest possible participation by the banks of the United States, whether members or nonmembers of the Federal Reserve System, in the financing contemplated under the authority of the President's Executive Order.

Under the Executive Order the three military procurement agencies are authorized to guarantee commercial banks, Federal Reserve Banks, the Reconstruction Finance Corporation, or other financial institutions against loss on loans made to concerns to finance the performance of war orders. The primary aim is to expand and expedite war production. Accordingly, peacetime credit rules or standards, as the President stated at the time of signing the Executive Order, must not be permitted to hold up production of war supplies needed by the armed forces.

The Board's Regulation authorizes the Federal Reserve Banks, acting in accordance with the provisions of the President's Executive Order and the instructions of the three military procurement agencies, to arrange loans and guarantees thereof wherever it is believed that they will

contribute to the obtaining of maximum war production expeditiously.

To assist in carrying out the provisions of the President's Executive Order and to aid in decentralizing operations under it as fully as possible, the War Department plans to have a liaison officer stationed at each Federal Reserve Bank. Generally speaking, the liaison officer will certify to the Reserve Bank that an applicant for financing is qualified from the technical or production standpoint to carry out a contract, subcontract or order for war supplies or equipment.

It is expected that any applicant will first take up his credit needs with his commercial bank or other financing institution. When the necessary credit cannot be arranged by the financing institution without the assistance of the War Department, the financing institution will apply to the Federal Reserve Bank for a guarantee of a part or all of the proposed financing. After certification by the liaison officer, it will be the Reserve Bank's function to analyze the financial aspects of the application, including the integrity of the management, and determine the type of financing best suited to meet the situation.

Under the initial instructions of the War Department, and upon appointment of liaison officers, guarantees or loans up to a prescribed maximum to be determined by the War Department will be made at the Federal Reserve Bank without reference to Washington.

Attached is a copy of Regulation V.

APPENDIX C.

Liaison Officer's Certificate to Federal Reserve Bank of Atlanta.

War Department
Washington, D. C.

Office of Liaison Officer,
Fiscal Division,
Federal Reserve Bank Building,
Atlanta, Georgia

SPBFR 6-156 October 31, 1942

Memorandum to: Federal Reserve Bank of Atlanta

Subject: Country Club Village Corporation
Mobile, Alabama

On behalf of the War Department and pursuant to the provisions of Executive Order No. 9112 of March 26, 1942, and the instructions from the War Department to all Federal Reserve banks, dated April 8, 1942, as modified, I hereby notify you that the Country Club Village Corporation, Mobile, Alabama, is engaged in a business or operation which is deemed to be necessary, appropriate or convenient for the prosecution of the War, and is in need of funds in order to facilitate or expedite war production.

/s/ J. Elliott Irvine,
J. Elliott Irvine,
Major, A. U. S.,
Liaison Officer.

JEI:mp

APPENDIX D.

Letter to Solicitor General.

Fyke Farmer
Attorney at Law
311 American Trust Building
Nashville, Tenn. 37201
Tel. 256-8506

Nov. 8, 1967

Hon. Erwin N. Griswold
Solicitor General of the United States
Department of Justice
Washington, D. C.

Re: Joseph W. Hart, et al. v. Federal Reserve Bank of Atlanta, Supreme Court No. 738

Dear Mr. Griswold:

You doubtless will assume from the fact that the Justice Department has defended this suit for the defendant, Federal Reserve Bank of Atlanta, and has been successful in procuring its dismissal, that the interests of the United States in some way are on the side of the Federal Reserve Bank. My purpose, as the attorney for the opposing side, is to call your attention to facts which I believe will cause you to conclude that the action of the Justice Department in defending the Federal Reserve Bank has been ill-advised and wrongful. I believe that you, as Solicitor General, will feel that you have the responsibility for making an independent decision as to where the interests of the United States are in this litigation, and that, upon investigation, you will conclude that the Federal Reserve Bank is liable to the United States for the loss it has suffered as the result of its unauthorized acts.

By reading the petition you will see that the War Department had no authority to guarantee the construction loan made by The First National Bank of Birmingham and The Merchants National Bank of Mobile to Country Club Village Corporation for a private residential subdivision. And, of course, it had no authority to purchase, pursuant to the guarantee agreement 90% of the unpaid balance of the indebtedness owing to the two banks by Country Club Village Corporation after application on the loan of the proceeds of the permanent F. H. A. financing. It is axiomatic that Federal Reserve Bank of Atlanta was without authority to act in the transaction as fiscal agent of the United States and bind the United States for the payment of funds for the acquisition of the 90% interest in the unpaid balance of the indebtedness.

As the interests of the United States could not be prejudiced, we may assume that, after the purchase of the 90% interest in the loan indebtedness held by the two Alabama banks, the United States was entitled to be substituted to the rights of the banks to the collateral securing the loan. And now we reach the nub of the matter, i. e., the wanton sacrifice of the security, the completed subdivision. Strangely enough, no claim has been made that The War Department and The Federal Reserve Bank of Atlanta, using their best judgment and acting in entire good faith for what they decided was the best interests of the United States, and The First National Bank of Birmingham and The Merchants National Bank of Mobile, also using their best judgment and acting in entire good faith for what they decided was the best interests of themselves and the debtor and its guarantors, the petitioners in the above captioned case, concluded that it was better to let the whole property go for a mere $37,000 than to keep it and collect the $150,000 unpaid balance from the rents and piece-meal sales of the 430 houses. Such a claim on their part would be tantamount to a con-

fession that they did not possess the business acumen of a real estate operator who turned his investment of $37,100 into a profit of more than $400,000.

But even if The War Department and the three banks had been willing to incur the disrespect and derision that a claim of a simple error in judgment would bring upon them they could not do so in face of the facts. The sale was made as of October 2, 1945. Prior to that time Mr. Hart, one of the petitioners, by letter proposed that the houses be placed on the market at $850.00 or $900.00 above the F. H. A. mortgage. He objected to a memorandum from The War Department suggesting that the houses be sold at approximately $500 above the individual F. H. A. Mortgages saying:

> "We feel that this price is too low, since a survey of Spring Hill Manor, Victory Place and Brookley Heights shows that a difference of from $900.00 to $1300.00 is charged above the mortgage and our suggestion would be that we place our houses on the market at $850.00 or $900.00 above the mortgage with a down payment of $500.00 and the balance to be absorbed over a period of say two years. I have talked to Colonel Irvine and he agrees with me on the price range."

Annexed hereto is a copy of Mr. Hart's letter dated April 7, 1945 addressed to Mr. John A. Hand, Vice President of The First National Bank of Birmingham. Copies of this letter were sent to Lt. Col. J. Elliott Irvine, the War Department liaison officer at Federal Reserve Bank of Atlanta, Mr. V. K. Bowman, Vice President of Federal Reserve Bank of Atlanta, and Mr. T. A. Horst, Vice President of The Merchants National Bank of Mobile.

The profit of $383,988.56 which Spring Hill Homes, Inc., the purchaser of the subdivision, realized from the piece-

meal sales of the houses is an average of approximately $900 per house.

I will not say yet that it is impossible for the Federal Reserve Bank of Atlanta and the two Alabama banks to prove that they did not intend to defraud the United States and Messrs. Hart and Russell, the guarantors of the Country Club Village Corporation indebtedness, but I do say that, on the facts now appearing, the conclusion that they acted from improper and corrupt motives in selling so valuable a property for a mere pittance is irresistible. I do not see how you can in good conscience defend the Federal Reserve Bank.

If I am mistaken about anything herein expressed, I will appreciate your letting me know about it. If I can be of any help to you, please call on me.

Yours very truly,

Fyke Farmer.

APPENDIX E.

Office of the Solicitor General
Washington, D. C. 20530

November 16, 1967

Fyke Farmer, Esq.
311 American Trust Building
Nashville, Tennessee 37201

Re: Hart et al. v. Federal Reserve Bank of Atlanta (No. 738)

Dear Mr. Farmer:

In further response to your letter of November 8, 1967, I wish to advise you that I have considered your views and have examined the proposed reply to your petition as prepared by attorneys of this Department. My conclusion is that the position previously taken by the government in this litigation is a correct one and that it should be maintained. You will shortly receive a copy of the brief elaborating our view of the matter.

Although, as I have indicated, I am unable to concur in your appraisal of the legal issues, I wish to thank you for your efforts in bringing your thoughts to my attention.

Very truly yours,

Erwin N. Griswold,

Erwin N. Griswold,
Solicitor General.